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No. 96-1592

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

October Term 1996

MARILYN OLKEY, *et al.*,

Petitioners,

v.

HYPERION 1999 TERM TRUST, INC., *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

RESPONDENTS' BRIEF IN OPPOSITION

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May 8, 1997

COUNTERSTATEMENT OF THE QUESTION PRESENTED

Whether a securities claim resting on an alleged material omission from a prospectus is dismissible under Fed. R. Civ. P. Rule 12(b)(6) when the prospectus in fact contains the allegedly omitted proposition?

STATEMENT PURSUANT TO SUPREME COURT RULE 29.6

This is to certify that respondents Hyperion 1997 Term Trust, Inc., Hyperion 1999 Term Trust, Inc., and Hyperion 2002 Term Trust, Inc. do not have any corporate parents or non-wholly owned subsidiaries.

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RESPONDENTS' BRIEF IN OPPOSITION

Respondents request that the Court deny the petition for a writ of *certiorari* seeking review of an opinion of the Court of Appeals for the Second Circuit reported at 98 F.3d 2 (2d Cir. 1996) (1a—citations herein to the opinions below are to the pages of the copies attached as an appendix to the petition).

COUNTERSTATEMENT OF THE CASE

The petition attacks the court of appeals for "decisions" the court never made on "issues" that were never presented. For example, petitioners define the question they wish this Court to address as: whether "express misrepresentations" regarding investment risks can somehow be "insulated from

liability" because of "generalized, 'implicit' cautionary statements that do not bear on the actual misrepresented risks"—a question that petitioners say the Second Circuit answered in the affirmative (Pet. i).

In reality, the court of appeals as well as the district court dismissed petitioners' complaint—not because of "generalized" statements or those failing to "bear on the" purportedly "misrepresented risk", as petitioners would have it—but because, as the appellate court itself stated: (1) the prospectuses "warn[ed] investors of *exactly* the risk the plaintiffs claim was not disclosed" (10a, emphasis added); (2) did so "explicitly", "fully" and "clearly" in "detailed" and "extensive" statements that were "too prominent and specific to be disregarded" (10a, 14a, 16a, 18a); (3) petitioners' averments were thus "contradicted by the prospectuses on their face" (4a); and (4) "therefore no set of additional facts could prove the plaintiffs' claims" (*id.*).

Petitioners' actual argument with the court of appeals decision consists of their assertion that the court somehow misread the prospectuses by failing to discern alleged errors and omissions. To create that impression, however, petitioners shut their eyes to the prospectuses' disclosures cited and quoted by the courts below and mischaracterize those documents as well as the court of appeals' opinion itself. In point of fact, both the court of appeals and the district court read the prospectuses correctly; but there is an even stronger reason why this petition should be denied.

The decisions below held that three prospectuses alleged to have misrepresented or omitted material facts were not actionable when revealed plainly on the face of the prospectuses themselves to have done neither. The rule of law underlying that holding is fully in conformity with this Court's precedents and the case law of other circuits; hence, no certworthy issue is presented.

A. Factual Background.

This is a securities case addressed to three prospectuses issued in connection with underwritings of stock in three separate investment trusts (Hyperion 1999 Term Trust, offered June 18, 1992 (A274-332);[1] Hyperion 1997 and Hyperion 2002, both offered October 23, 1992 (A333-403 and A404-474, respectively)). As is typical of underwriting prospectuses, those at issue in this case contained statements of aspiration and opinion as to possible future gains as well as statements of the risks necessarily to be hazarded before any such gains might be realized.

As to possible gains, the prospectuses stated the goals of achieving

> "a higher level of current income than could be obtained by investing in a portfolio of intermediate-term (five- to ten-year) U.S. Treasury securities . . . ." (Hyperion 1999 at A276, 287-88; 2002 at A409, 423; *see* Hyperion 1997 at A338, 352)

and returning, at the termination of each Trust each shareholder's initial investment of $10 a share (*e.g.*, Hyperion 1999 at A274; 1997 at A335; 2002 at A406).

As for warnings, the prospectuses stated, among many other expressions of risks, that, to earn income greater than that generated by investing in a portfolio of medium-range U.S. Treasuries, the Trusts would invest primarily in mortgage-backed securities, with as much as 25-35% of the total Trust investment in IOs (a security representing the right to receive the interest portion of a pool of mortgages) (Hyperion 1999 at A280, 288, 302; *see* 1997 at A343, 352, 367; 2002 at A414, 423, 437); that, if interest rates fell, there would likely be more prepayments of the underlying

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[1] "A" citations are to pages of the joint appendix filed in the Second Circuit.

mortgages than would otherwise be the case, which would reduce the flow of interest income to security-holders (Hyperion 1999 at A284, 300-01, 301-02, 1997 at A348, 365-66, 366-67; 2002 at A418-19, 436, 437); and that, with these kinds of securities, if such mortgage prepayments occurred, the Trusts (and, necessarily, their investors) could "fail to recoup their initial investment", in addition "to suffer[ing] a lower than anticipated yield" (Hyperion 1999 at A290; 1997 at A354; 2002 at A425).

Those statements were made in June 1992 in the Hyperion 1999 prospectus (and in October 1992 in the 1997 and 2002 prospectuses) when home mortgage interest rates had already fallen to an 18-year (or 19-year) low. As is now known, with the benefit of hindsight, those rates thereafter fell to their lowest point since FHLMC began compiling weekly interest rates in 1971.[2] Hence prepayments of mortgages occurred, and the Trusts' net asset values ("NAVs") and share prices declined. In other words, there transpired some of the ill consequences the prospectuses predicted could result *if* interest rates continued to go down.

B. Petitioners' Shifting Theories of the Case.

According to petitioners' third generation of pleadings (the second consolidated amended complaint), the prospectuses in question constituted violations of either or all of Sections 11, 12(2) and 15 of the '33 Act and Sections 10(b) (including Rule 10b-5) and 20(a) of the '34 Act and amount to common-law fraud.

These charges were originally inspired, it would appear, by opinions expressed by a *Barron's* columnist in an article dated October 18, 1993 (Pet. 2-3). Before that day ended, the

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[2] For each of five consecutive weeks, beginning in February 1993, rates fell to new 20-year lows, culminating at 7.44%. Then, in July 1993 and continuing until this suit was commenced in October 1993, interest rates fell even further, hitting a new recorded low of 6.81%.

first of what turned out to be 16 securities class action complaints was filed against the Trusts, their investment advisor, various directors and officers and an asserted defendant class of underwriters. The complaints were largely identical, and all accused the Trusts of failing to disclose to investors that the Trusts would make "huge" purchases of IOs and that such securities tend to lose value when interest rates decline (*e.g.*, A481-95, ¶¶ 18-20). The plain fact was, however, that the prospectuses had elaborately described the nature and risks of IOs as well as the extent to which the Trusts would invest in such securities. By the time plaintiffs filed their first amended complaint, they presumably had sufficient opportunity so to realize, since they then abandoned this argument in favor of a new, more generalized theme relating to the entirety of the portfolios.

Petitioners' theory of the case thereafter underwent additional radical shifts, expressed in yet another round of pleadings and various briefs and arguments to the courts below. The present petition emphasizes, as did plaintiffs' oral argument to the court of appeals, one of the themes set forth in the latest version of the complaint—specifically, that while the prospectuses warned that significant declines in interest rates could cause reductions in Trust income, it purportedly gave no such warning with regard to the comparable vulnerability of Trust capital (*e.g.*, Pet. 6).

C. The Decisions Below.

Both the district court and the court of appeals found that the prospectuses clearly and unambiguously informed investors of precisely the proposition that petitioners assert had been misrepresented or omitted.

The district court noted that the "prospectuses disclosed that a decline in interest rates could trigger a deluge of mortgage prepayments" and that such "prepayment[s] could produce an irretrievable loss of capital" (39a); that "the risks threatening capital were revealed" with "candor" (41a); and

that "[n]o investor could have believed that net asset values would not be volatile and capital would not be vulnerable unless that investor deliberately ignored [those] explicit warnings" (43a). The court of appeals observed, based on the same warnings, that the "risks involved" were "fully and explicitly disclosed" (16a) so that the "prospectuses contained no material misstatements or omissions of fact" (19a). Thus, the courts below ruled that the second amended consolidated complaint failed to state a claim upon which relief could be granted and dismissed it.

CORRECTION OF MISSTATEMENTS IN THE PETITION

Petitioners' theory of the existence of a certworthy issue is that (1) the prospectuses misrepresented that there would be little or no risk of capital loss as a consequence of declining interest rates (Pet. 6), (2) their warnings were "vague" and "generalized" "boilerplate" that did not go to that risk (Pet. 14-15), and (3) the court of appeals improperly "speculated" that investors would interpret such "boilerplate" as warnings that did go to that risk (Pet. 17).

Each of those assertions self-evidently misstates the record.

A. The Petition's Assertion of "No Warning" of "Risk to Investor Capital"; the Plain Existence of Such Warnings.

1. The prospectuses stated that the Trusts would design and manage each portfolio "in an *attempt* to minimize the impact of changes in interest rates on the net asset value of the portfolio" (9a, emphasis added). Also, as the petition itself expressly acknowledges, "[e]ach prospectus warned of a possible decrease in the Trusts' yield if interest rates should decline 'significantly'" (Pet. 6). But, say petitioners, "[t]here was no warning given of any corresponding risk to investor capital"—and that, according to petitioners, was a material

omission that rendered the first statement a misrepresentation (*id.*).

That alleged omission is petitioners' case. It is the supposed platform for all petitioners' hyperbole regarding "secret" "bets" on interest rates, hidden "risky" strategy, and so forth. But, as the courts below found with ample basis, there was no such omission.

Each prospectus stated plainly and repeatedly about each Trust portfolio:

> *one*, that it would be composed primarily of mortgage-backed securities (34a);
>
> *two*, that what depressed the market value of mortgage-backed securities were prepayments of the underlying mortgages;[3]

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[3] *E.g.*:

"S&P and Moody's determine ratings for Mortgage-Backed Securities . . . . The ratings do not represent an assessment of the likelihood that principal prepayments will be made by mortgagors or other obligors, which may cause investors to suffer a lower than anticipated yield or fail to recoup their initial investment." Hyperion 1999 at A290; 1997 at A354; 2002 at A425.

"The investment characteristics of Mortgage-Backed Securities differ from traditional debt securities. The major differences include the fact that . . . principal may be prepaid at any time . . . . These differences can result in significantly greater price and yield volatility than is the case with traditional debt securities. As a result, if the Trust purchases Mortgage-Backed Securities at a premium, a prepayment rate that is faster than expected will reduce both the market value and the yield to maturity from that which was anticipated . . . ." Hyperion 1999 at A279; 1997 at A341-42; 2002 at A412.

three, that what caused mortgage prepayments was declining interest rates;[4]

four, that, if the Trust used leverage, the negative impact on the entire Trust net asset value ("NAV") would be magnified;[5] and

five, that the Trust would, in fact, use leverage.[6]

To be sure, the expression of those propositions did not use the words "bias toward a rising interest rate environment"—a fact (together with the court of appeals' description of that conclusion as being "implicit") to which petitioners attach great importance (Pet. 14-15). But once a prospectus states, as these unmistakably did, that the NAV of

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[4] *E.g.*:

"Prepayment rates are influenced by changes in current interest rates . . . In periods of declining mortgage interest rates, prepayments on Mortgage-Backed Securities generally increase." Hyperion 1999 at A300; 1997 at A365-66; 2002 at A436.

[5] *E.g.*:

"The use of leverage by the Trust . . . creates special risk . . . . [S]ince any decline in the value of the Trust's investment portfolio is borne entirely by the holders of the Shares, the use of leverage in a declining market will cause a greater decline in the asset value of the Shares than if the Trust were not leveraged." Hyperion 1999 at A302-03; 1997 at A367-68; 2002 at A438.

"[L]everaging may magnify changes in the net asset value of the Shares." Hyperion 1999 at A281; *see* 1997 at A345; 2002 at A415.

"The use of leverage poses the additional risk that . . . decline in the value of the Trust's investment portfolio may exaggerate the decline in the net asset value or market price of the Shares." Hyperion 1999 at A283; 1997 at A347; 2002 at A418.

[6] *E.g.*:

"The Trust intends to use investment leverage." Hyperion 1999 at A283; 1997 at A347; 2002 at A418.

a portfolio of securities will decline in a declining interest rate environment, the concept that the portfolio has a bias towards a rising interest rate environment is not only "implicit"; the two statements are alternative verbalizations of the same point.

That is why the court of appeals also stated that, while the word "bias" wasn't used, the warning itself of vulnerability to declining interest rates was "fully and explicitly disclosed" (16a) in an "unmistakable" fashion (13a) that was "too prominent and specific to be disregarded" (10a). Obviously, what matters is that the risk be disclosed, not that one formulation of words rather than another be articulated.

2. Moreover, what, other than precisely the warning petitioners claim wasn't given, was the following passage in the context of prospectuses addressed to portfolios said to be invested in mortgage-backed securities and only to "a limited amount"[7] in anything else:

> "The investment characteristics of Mortgage-Backed Securities differ from those of traditional debt securities. The major differences include the fact that, on Mortgage-Backed Securities . . . prepayments of principal may be made at any time. Prepayment rates are influenced by changes in current interest rates and a variety of economic, geographic, social and other facts and cannot be predicted with certainty. *In periods of declining mortgage interest rates, prepayments on Mortgage-Backed Securities generally increase. . . . Under certain interest rate or prepayment rate scenarios, the Trust may fail to recoup fully its investment in such securities notwithstanding the assignment of a rating of AAA to such securities.*" Hyperion 1999 at A300-01; 1997 at A365-66; 2002 at A436 (emphasis added).

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[7] Hyperion 1999 at A274; 1997 at A335; 2002 at A406.

And surely the statement on page 2 of each prospectus that "[c]hanges in interest rates *will* also lead to changes in the Trust's net asset value" (emphasis added) immediately coupled with the warning that the Trust could suffer so substantial a negative change in net asset value as to be forced "to return less than $10 a share" also constituted such a warning (Hyperion 1999 at A275; 1997 at A336; 2002 at A407).[8]

Likewise, in each prospectus the statement was made that, while the Trust will "seek to minimize the impact" on "the net asset value" caused by "changes in interest rates", "there can be no assurance that it will achieve this result" (Hyperion 1999 at A284; 1997 at A348; 2002 at A418). What else could such a statement mean than: if the Trust does *not* "achieve this result" of which "no assurance" can be given, interest rate changes could well bring about reductions in the net asset value of the Trust?

Indeed, every time the prospectuses warned that the Trusts or the Trusts' Adviser will "*attempt*" to prevent such a reduction in NAVs (and such are the very passages most frequently quoted in this second amended complaint, *e.g.*, paras. 47, 56, 57), the message was undeniably delivered that the "attempt" might not succeed; and then the prospectuses

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[8] In isolation and out of context, the statement that interest rate changes will change the portfolio's NAV would be "vague", as the court of appeals noted, as to the direction of those changes (13a). Petitioners seize upon the word "vague" as they did with the word "implicit" and equally misuse it (Pet. 14), making it appear that it was a general court of appeals' description of warnings that the court itself described as "specific", "explicit", "full", "appropriate", "prominent", etc (*e.g.*, 10a, 16a). Not only, however, did the court of appeals limit the word, as the court itself stated, to the hypothetical condition of this one sentence standing "*by itself*", but it went on to state that placing this sentence *in context* ("the juxtaposition of the two sentences") "creates an unmistakable inference that a drop in interest rates could decrease net asset value" (13a, emphasis added).

so stated explicitly (*e.g.*, Hyperion 1999 at A277, 280 284 (twice), 288, 289; 1997 at A338, 343, 348, 349, 352, 353; 2002 at A409, 413-14, 418-19, 419-20, 423, 424).

3. Petitioners' response is that such explicit and particularized warnings should be disregarded as "boilerplate" in the light of the statements in the prospectuses regarding "balance" (Pet. 15).[9] However, what the prospectuses said about "balance" was that the Trust managers would attempt to achieve it; that such efforts might not succeed because of market forces beyond their control, *including interest rate drops causing prepayments*; that nobody should rely on it being achieved; and that the failure of achievement could result in a capital loss (*i.e.*, the return of less than $10 a share upon the Trust's liquidation). In that context, the above-quoted statements, far from being meaningless "boilerplate", were clear explications of how such capital losses could occur.

B. The Petition's Assertion that the Court of Appeals "Speculated" as to "What Plaintiffs Might Have Believed and Must Have Expected"; the Court's Reading of Clear Words to Rule on the Prospectuses' Plain Meaning.

1. When a court determines that an accused publication is not susceptible of a defamatory meaning, the court properly dismisses a libel complaint (*e.g.*, *Chapin v. Knight-Ridder, Inc.*, 993 F.2d 1087, 1091 (4th Cir. 1993); *Mitchell v. Random House, Inc.*, 865 F.2d 664, 669 (5th Cir. 1989); *Fudge v.*

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[9] The prospectuses themselves never used the word "balance", but rather stated in various ways that an "attempt" would be made "to minimize the impact of changes in interest rates on the net asset value of the portfolio", such as by purchasing securities that tend to react in different ways to given interest rate changes (Hyperion 1999 at A277; 1997 at A338; 2002 at A409). We have no objection to the use of the word "balance" as a shorthand reference to such statements (although plaintiffs' usage seems erroneously to imply an ability to achieve "balance" in some mechanical and foolproof fashion).

Penthouse Int'l, Ltd., 840 F.2d 1012, 1015-16 (1st Cir. 1988)). When a court determines that a prospectus contains a proposition it is claimed to have omitted, the court properly dismisses a complaint for a purported securities violation.

In the libel case, the court applies a reasonable reader standard, and in the securities case, a reasonable investor standard (*see Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988)). In neither instance does the court "speculate" (to use petitioners' word) as to how any particular person would read the document. In both cases, the court renders a ruling of law based on facts it finds not reasonably contestable.[10]

That is precisely what the district court did when it stated that "[n]o investor could have believed" from reading these prospectuses that "capital would not be vulnerable" in a declining interest rate environment (43a). To the same effect was the court of appeals' conclusions regarding the beliefs that "[r]easonable investors" would necessarily have about "risking low returns and erosion of capital if there was a significant drop in interest rates" (14a).

These conclusions were not "speculation" (much less "conceded speculation") about "what plaintiffs might have believed" or what any particular investor "might have believed", as petitioners characterize them (Pet. i, 3, 17); they were, as the court itself made evident, conclusions as to what these prospectuses were clearly stating and thus, objectively, what reasonable investors would necessarily have understood. Indeed, based on even the brief summary of the prospectuses set forth above, those conclusions were ineluctable.

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[10] And this practice is, of course, not unique to libel and securities claims. *See, e.g., Venture Assocs. Corp. v. Zenith Data Systems Corp.*, 987 F.2d 429, 432-33 (7th Cir. 1993) (dismissal of complaint for alleged breach of contract, where the executed documents showed on their face an agreement to agree rather than an enforceable contract).

2. The dissenting opinion in the court of appeals, on which petitioners heavily rely, missed exactly the same point. To the dissent, the majority had "assert[ed]" "in the absence of evidence, that the *purchasers* of the Hyperion funds bought in the expectation of rising [interest] rates"—which the dissent considered "a proposition at least unsupported and in all likelihood unsupportable" (23a, emphasis added).

In the first place, however, as noted above, the court of appeals rendered an objective reading of the prospectus, not a divination of the minds of particular purchasers. In the second place, the majority determined (and not even the dissent disagreed) that these prospectuses made clear to any "reasonable investor" that both the capital and income of the Trust would fare better in a rising interest rate environment than if rates were to fall (14a). In so stating, therefore, the majority indulged in neither "speculation" nor "unsupportable" assumptions, but rather clear comprehension of the plain words of the prospectuses, and the application of common sense.

C. The Petition's Assertion of "Illogical" Speculation; the Illogical Speculation on Which the Assertion is Premised.

While the dissenting opinion mistakenly chided the majority for "speculation" (22a), it ironically embarked upon impermissible speculation of its own (which the petition, of course, endorses).

According to the dissent (and petition), the Trust managers had invested so "disproportionately in instruments that would benefit from rising [interest] rates" (20a-21a) that their "aim" could not possibly have been "for as much balance as [they could] achieve" (24a; Pet. 5 & n.3). The basis for this conclusion was that other "closed-end bond fund[s]" did better than Hyperion's in the opinion of a *Barron's* columnist (21a; Pet. 2)—a reference that fails not only as appropriate authority but, more importantly, as logical support.

In essence, the dissent's argument is a hindsight contention that, since the attempt failed, it must never have been made or even intended. And the fallaciousness of that position is all the more ironic in the light of the dissent's acknowledgement of the majority's point that even "portfolio managers of funds claimed to be balanced must inevitably make some predictions about future interest rates" because "it is unlikely that interest rates will remain completely static for any significant period of time" (26a).

For the dissent's statement presupposes that fund managers must make some "bet" on which way interest rates will move. And since the predictions of different managers will invariably be different, they will achieve different results despite the commonality of their "aim". Moreover, these Trusts were to be invested heavily, as the prospectuses continuously stated, in a relatively new form of security, IOs, whose precise reaction to interest rate changes, and to the other market and economic effects of those changes, could not yet have been fully charted. To cite, then, the experience of *other* investment trusts as a purported basis for the assertion that the Hyperion Trusts were "disproportionately" "bet" on an interest rate movement (26a) is to advance not simply hindsight reasoning but a complete *non sequitur*.

All that could be said with certainty at the outset was that these mortgage-backed securities were vulnerable to the prepayment risk caused by declining interest rates; the Hyperion prospectuses so stated repeatedly; and the risks of which they warned were the risks that ultimately eventuated. That should have been, and in the majority's view properly was, the end of this lawsuit.

D. The Petition's Assertion of a Promised "Conservative" Investment; the Prospectuses' Explicit Warnings to the Contrary.

Typical of petitioners' approach to the prospectuses is their repeated claim that respondents "represented that they

had assembled portfolios designed for conservative investors" (Pet. 2), emphasized to the public that the Trusts were investments of a "conservative nature" (*id.*), made "[t]he promise of a conservative, capital protective approach" (Pet. 5), made "representations of a conservative strategy" (Pet. 6), advertised a "conservative" product (Pet. 15), and so on.

These arguments make it appear as though the prospectuses had the word "conservative" blazoned throughout their pages like a mantra. Not so. The prospectuses *never* described their offerings as "conservative", nor did they communicate such a message by implication (which is probably petitioners' point).

Surely, for example, there was no implication of a "conservative" investment when the prospectuses said, in plain English, that the objectives might well *not* be met[11] and that $10 a share might well *not* be returned.[12] And certainly there was no such implication when the prospectuses stated that the Trusts would invest as much as 25% to 35% of each portfolio in securities (IOs) that could lose their value, irrespective of their triple-A rating, if the underlying mortgages were prepaid and that such refinancings "generally" occur when interest rates decline.[13] And manifestly there was no invitation to only risk-adverse buyers when the

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[11] Hyperion 1999 at A275, 276; 1997 at A336, 337; 2002 at A407, 408 ("No assurance can be given that the Trust will achieve its investment objectives."); *accord* 1999 at A286, 287; 1997 at A350, 351; 2002 at A421, 422.

[12] Hyperion 1999 at A275, 276; 1997 at A336, 337; 2002 at A407, 408 ("[T]he Trust may return less than $10.00 per Share"); *see* Hyperion 1999 at A283, 286, 287, 289; 1997 at A347, 350, 351, 353; 2002 at A418, 421, 422, 424.

[13] Hyperion 1999 at A280, 284, 288, 290, 294, 300, 301, 301-02; 1997 at A343, 348, 352, 354, 359, 365-66, 366-67; 2002 at A414, 418-19, 423, 425, 429, 436 (twice), 437.

prospectuses expressly warned that, given the *stated* risks, these Trusts were "not appropriate for all investors" and that, before investing, those interested "should carefully consider their ability to assume these risks".[14]

In short, "conservative" is petitioners' word; arguments and claims founded on that concept are petitioners' own invention; they have no foundation in the prospectuses themselves.

REASONS FOR DENYING THE WRIT

1. Contrary to petitioners' assertion, the decision below was not based on the "bespeaks caution" doctrine, much less on "cautionary statements" unrelated to the allegedly omitted disclosure of risk (Pet. i). Rather, the dismissal, as the court of appeals itself stated expressly, was based on the clear fact that the prospectuses contained the very statements that "warn[ed] investors of exactly the risk the plaintiffs claim was not disclosed" (10a).

Whether brought under Sections 11 or 12(2) or Rule 10b-5, complaints charging "omissions" of what was disclosed, or "misrepresentations" that were not stated, are themselves deficient. *E.g.*, *I. Meyer Pincus & Assocs., P.C. v. Oppenheimer & Co.*, 936 F.2d 759, 762-63 (2d Cir. 1991); *In re Stac Electronics Sec. Litig.*, 89 F.3d 1399, 1405-06 (9th Cir. 1996), *cert. denied*, ___ U.S. ___, 117 S.Ct. 1105 (1997); *Decker v. Massey-Ferguson, Ltd.*, 681 F.2d 111, 115-17 (2d Cir. 1982). The same rule applies whether the allegedly omitted (but, in reality, stated) proposition is one of fact (as in the above-cited cases) or an appraisal of the riskiness of the security in question. *E.g.*, *Luce v. Edelstein*, 802 F.2d 49, 56 (2d Cir. 1986). No clearer example could be presented for the application of that rule than the second amended complaint filed in this action.

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[14] Hyperion 1999 at A304; 1997 at A369; 2002 at A440.

Whenever the second amended complaint alleges or implies something was omitted from the prospectuses, the supposedly omitted proposition can be found stated, not once, but frequently. And each time the second amended complaint attempts to characterize the prospectuses as containing a misrepresentation, the prospectuses themselves belie the characterization.

There are a lot of cases endorsing the "bespeaks caution" doctrine (*see, e.g.*, *Pincus*, 936 F.2d at 763; *Gasner v. Board of Supervisors*, 103 F.3d 351, 358 (4th Cir. 1996); *In re Syntex Sec. Litig.*, 95 F.3d 922, 929-30 (9th Cir. 1996)). And these prospectuses, as the courts below properly held, bespeak caution (10a, 42a)—but we are far beyond that doctrine here, as the lower courts also recognized. This is a case in which petitioners' purported bases for their suit are mischaracterizations demonstrable on the face of the very documents under which they are claiming.

2. Petitioners assert, as if it were self-evidently the case, that these prospectuses gave "no warning" of any risk "of a possible decrease in the Trusts'" capital "if interest rates should decline 'significantly'" (Pet. 6). The stark reality, however, is otherwise. Petitioners have simply blinded themselves to what the prospectuses manifestly set forth and the court of appeals properly understood.

When prospectuses state, as these did, that investors may fail to recoup their investment in mortgage-backed securities when large prepayments are caused by declining interest rates and that the portfolio of the Trust will consist primarily of such securities and only to "a limited amount" anything else, indisputably a warning has been issued "of a possible decrease in the Trusts'" capital "if interest rates should decline 'significantly'" (Pet. 6). And when prospectuses state, as these did, that the mortgage-backed securities of which the portfolios would be predominantly composed can be depressed in value by mortgage prepayments that are caused

by declining interest rates, a phenomenon magnified and exaggerated when leverage is used—and that this Trust intends to use leverage—such a warning has undeniably been issued.

In so holding, the court of appeals neither departed in any way from precedents of this Court nor rendered an opinion conflicting with the case law of other circuits. The decision it reached was that the claim petitioners had attempted to state was refuted on the face of their pleading, which was a straightforward application of Rule 12(b)(6) in exactly the manner the Rule was intended to be used.

3. Petitioners' assertion that the court of appeals "speculated" as to how shareholders might have read the prospectuses misdescribes the court of appeals' opinion; and petitioners' reliance on their own affidavits is simply misplaced.

As mentioned above, it is as appropriate under Rule 12(b)(6) for a court to determine whether a prospectus actually omits or contains the allegedly missing material disclosures as it is for a court to determine whether an allegedly libelous publication is susceptible of a defamatory meaning. In neither instance is the court "speculating", much less engaged in some improper deprivation of Seventh Amendment rights. It can no longer be seriously challenged that for plaintiff to possess a right to have his or her claim resolved by a jury, he or she must be able to state a claim on the face of a pleading, which is not done where, as the court of appeals held here, "plaintiffs' claims are contradicted by the prospectuses on their face" (4a).

Nor do petitioners' own self-serving affidavits remove them from this sound precedent. Petitioners can proclaim as often or as loudly as they wish that these prospectuses failed to warn them of risks to capital (*e.g.*, Pet. i, 3-4, 8, 17), but the plain words of the prospectuses say otherwise. Affidavits cannot change that stark fact, nor are the courts below

required on a Rule 12(b)(6) motion to accept them as changing that fact.

In sum, the ruling of the courts below that these securities claims could not be founded on prospectuses clearly containing the disclosures they were alleged to have omitted was correct, in full conformity with prior law and in no respect worthy of the grant of *certiorari*.

CONCLUSION

For the foregoing reasons, the writ of *certiorari* should be denied.

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Respectfully submitted,

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